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International Accounting Harmonization:

Evidence from Europe

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Abstract: The goal of this study is to describe and summarize how the harmonized international accounting system can promote business decisions and influence economic environment. The unified, harmonized accounting system will lead to new types of analysis and data, furthermore with the possible integration of new indicators from the business management of certain countries. Especially the multinational companies whose subsidiaries had to report for some purposes using national accounting rules convert and consolidate their different framework for unified financial statement where they are listed. A suitable international accounting system can help multinational enterprises accomplish their managerial functions on a global basis. Meanwhile the interpretation and adoption of the financial information based on the different accounting methods are also expensive for the users of these reports. Therefore an authentic and harmonized international accounting system could form that business language, which would allow the comparison of the accounting information of each country. The accounting system differences matter even to financial analysts who specialize in collecting, measuring and disseminating business information about the covered companies suggests that there are potential economic costs, associated with variation in national rules across countries. Besides, it is very important task for managers and researchers the valuation and analyzing the effects of harmonized accounting system on the business environment, especially their contribution to globalization. According to the business practice it is obvious that the usage of harmonized international accounting system leads to a reduction of the information asymmetry between the owners and the managers.

Key words: accounting harmonization; globalization; classification; national rules differences; influencing factors; Europe

1. INTRODUCTION

The purpose of the use of international accounting systems is that similar accounting transactions are treated the same by companies around the world, resulting in globally comparable financial statements.

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However, using the unified accounting information system consistently by firms we will find that they are changeable, because they are depend on the varying economic, political, and cultural conditions in one state. Accountants, auditors and information scientists around the globe are planning to harmonize accounting information systems with the goal of creating one set of high-quality accounting rules to be applied around the world.

With increasing globalization of the marketplace, international investors need access to financial information based on harmonized accounting systems and procedures. Investors constantly face economic choices that require a comparison of financial information. Without harmonization in the underlying methodology of financial reports, real economic differences cannot be separated from alternative accounting systems and procedures. Harmonization is used as a reconciliation of different points of view, which is more practical than uniformity, which may impose one country's accounting point of view on all others. With the growth of international business transactions by private and public entities, the need to coordinate different investment decisions has increased. This would also lead to the reduction of the information diversity between managers and investors. The information diversity is a costly and can be blamed for the decrease of the managers' bonus, the increase of the equity's cost and the inaccuracy of the economical and the financial forecasts

Historically, harmonization of the international accounting information systems has tended to follow the integration of the markets served by the accounts. For example, the move to unified national accounting system in the US in the early 20th century followed the integration of the national economy. Similarly, the present impetus for global accounting information system follows the accelerating integration of the world economy. Without the common accounting system the cross-border portfolio and direct investment may be distorted, the monitoring of management by shareholders obstructed, the contracting inhibited and the cost of these activities may be needlessly inflated by complex translation (Meeks and Swann, 2009).

According to the business practice it is obvious that the usage of harmonized international accounting system leads to a reduction of the information asymmetry between the owners and the managers. By this information asymmetry are growing the costs of equities and are less accurate the economical and financial forecasts. This requires the development and review of the national accounting rules, the separate validation of the tax and accounting regulation, the repeal of the subordinate role of accounting, issuing international standards with the help of practical and theoretical accounting experts.

Since in case such multinational companies like Daimler Chrysler owning more than 900 subsidiaries, operating in 5 continents in more than 60 countries, the published financial results according to international accounting system is 1.5 times of the one according to German accounting rules. If earning after taxation (EAT) – deducted actual tax burdens - according to US GAAP (Generally Accepted Accounting Principles) is taken as 100 percent, due to differences between national accounting rules, EAT would be 25% more in UK, 3% less in France, 23% fewer in Germany and 34% less in Japan (Barth et al., 2007).

2. PREVIOUS RELATED LITERATURE

International accounting literature provides evidence that accounting quality has economic consequences, such as costs of capital (Leuz and Verrecchia, 2000), efficiency of capital allocation (Bushman and Piotroski, 2006) and international capital mobility (Guenther and Young, 2002).

Epstein (2009) compared characteristics of accounting amounts for companies that adopted IFRS (International Financial Reporting Standards) to a matched sample of companies that did not, and found that the former evidenced less earnings management, more timely loss recognition, and more value relevance of accounting amount than did the latter. This study found that IFRS adopters had a higher frequency of large negative net income and generally exhibited higher accounting quality in the post-adoption period than they did in the pre-adoption period. The results suggested an improvement in accounting quality associated with using IFRS.

Botsari and Meeks (2008) found that first time mandatory adopters experience statistically significant increases in market liquidity and value after IFRS reporting becomes mandatory. The effects were found to range in magnitude from 3 to 6% for market liquidity and from 2 to 4% for company by market capitalization to the value of its assets by their replacement value.

Daske et al. (2007) also found that the capital market benefits were present only in countries with strict enforcement and in countries where the institutional environment provides strong incentives for transparent filings. In the order of the IFRS adoption countries, market liquidity and value remained largely unchanged in the year of the mandate. In addition, the effects of mandatory adoption were stronger in countries that had larger differences between national GAAP (General Accepted Accounting Principles) and IFRS, or without a pre-existing convergence strategy toward IFRS reporting.

The increased transparency promised by IFRS also could cause a similar increase in the efficiency of contracting between firms and lenders. In particular, timelier loss recognition in the financial statements triggers debt covenants violations more quickly after firms experience economic losses that decrease the value of outstanding debt (Ball and Shivakumar, 2005; Ball and Lakshmann, 2005).

Accounting theory argues that financial reporting reduces information asymmetry by disclosing relevant and timely information for example Frankel and Li (2004). Because there is considerable variation in accounting quality and economic efficiency across countries, international accounting systems provide an interesting setting to examine the economic consequences of financial reporting. The European Union’s (EU) movement to IFRS may provide new insights as firms from different legal and accounting systems adopt a single accounting standard at the same time. Improvement in the information environment following change to IFRS is contingent on at least two factors, however. First, improvement is based upon the premise that change to IFRS constitutes change to a GAAP that induces higher quality financial reporting. For example, Ball et al. (2006a) found that the accounting system is a complementary component of the country’s overall institutional system and it is also determined by firms’ incentives for financial reporting. Second, the accounting system is a complementary component of the country’s overall institutional system (Ball et al., 2006b) and is also determined by firms’ incentives for financial reporting. La Porta et al. (1998) provide the first investigation of the legal system’s effect on a country’s financial system. The results suggested that common law countries have better accounting systems and better protection of investors than code law countries.

Other factors associated with financial reporting quality include the tax system (Daske and Gebhardt, 2006), ownership structure (Jermakovicz et al., 2007, Burgstahler et al., 2006), the political system (Li and Meeks, 2006), capital’s structure and capital market development (Ali et al., 2000). Therefore, controlling for these institutional and firm-level factors becomes an important task in the empirical research design. As a result of the interdependence between accounting standards and the country’s institutional setting and firms’ incentives, the economic consequences of changing accounting systems may vary across countries. Few papers have examined how these factors affect the economic consequences of changing accounting standards. For example, Pincus et al. (2007) found that accrual anomaly is more prevalent in common law countries. Maskus et al. (2005) found that accounting quality is associated with tax reporting incentives. Exploration of the interaction between these factors and the accounting information system can provide insights into differences in the economic consequences of changing accounting principles across countries.

Prior researches, for example, Meeks and Meeks (2002) have raised substantial doubt regarding whether a global accounting standard would result in comparable accounting around the world. But differences in accounting practices across countries can result in similar economic transactions being recorded differently. This lack comparability complicates cross-border financial analysis and investment. In the researches of Iatridis and Rouvolis (2010) are some evidence of earning management (e.g. reducing of transition costs and information asymmetry, benefits of investors in investment strategy). They showed how firms that operate in a non-common-law countries (e.g. Greece), which is stakeholder-based respond to international accounting standards adoption as compared to shareholder-based systems (e.g. United Kingdom).

No matter how similar the accounting systems in different countries are, there will be slight or even bigger differences in the way they are applied by companies due to the differences in the economical, political and cultural environment. Chatterjee (2006) presented in his study how cultural differences can affect accounting practices is that in the countries which are characterized with small power distance and weak uncertainty avoidance accounting measures are more likely to be used as an indicator of a manager's performance than as a measure of the effectiveness of policies and procedures prescribed for them. Various researches draw the conclusion that countries having different cultures have also different accounting rules and practices.

3. CLASSIFICATION OF ACCOUNTING SYSTEMS

In this paper "accounting system" would be used as the financial reporting practices used by a company for an annual report. The systems could be classified into groups by similarities and differences. If all or most of the enterprises in a country are employed by very similar accounting practices, this might suggest that countries can be classified on the basis of accounting practices.

The classification of accounting systems should help to describe and compare international accounting systems in a way that will promote improved understanding of the complex realities of accounting practice. This classification should contribute to an improved understanding of:

- the extent to which national accounting systems are similar to or different from each other,
- the pattern of development of individual national systems with respect to each other and their potential for change,
- the reasons why some national systems have a dominant influence while others do not.

Classification should also help policymakers assess the prospects and problems of international harmonization. Developing countries seeking to choose an appropriate accounting system will also be better informed about the relevance for them of the systems used by other countries. The education of accountants and auditors who operate internationally would also be facilitated by an appropriate classification system.

The next hypothetical classification by Doupnik and Perera (2007) based on some explanatory variables for differences in measurement practices.

Classes:

- micro-fair-judgemental and commercially driven,
- macro-uniform government-driven and tax-dominated.

Sub-classes:

- business economics and extreme judgemental (Netherlands),
- business practice, professional rules and British origin.

Families:

- UK influenced and professional regulated (Australia, New-Zealand, UK, Ireland),
- US influenced and enforcement by SEC (Canada, Israel, USA).
- code-based and international influenced (Italy),
- plan-based (France, Belgium, Spain),
- statue-based (Germany, Japan),
- economic controlled (Sweden).

All attempts were made to isolate those features of a country's financial reporting practices that may constitute long-run fundamental differences between countries. The result was a selection of nine factors:

- type of users of the published accounts of listed companies,
- degree to which law or standards prescribe in detail and exclude judgement,
- importance of tax rules in measurement,
- conservatism/prudence (e.g. valuation of assets),
- strictness of application of historical cost (in the historical cost accounts),
- susceptibility to replacement cost adjustments in main or supplementary accounts,
- consolidation practices,
- ability to be generous with provisions (as opposed to reserves) and to smooth income,

♦ uniformity between companies in application of rules.

Connections:

- micro-fair-judgemental and commercially driven class covers two sub-classes:
  - -- business economics and extreme judgemental,
  - -- business practiced, professional rules and British origin.
- macro-uniform, government-driven and tax-dominated class contents four families:
  - -- code-based and international influenced,
  - -- plan-based,
  - -- statue-based,
  - -- economic controlled.

The micro-fair-judgemental and commercially drives class is also known as the Anglo-Saxon or Anglo-American model, used to describe to approach of the United Kingdom and United States, where accounting is oriented toward the decision needs of large numbers of investors and creditors. This model is employed by most English-speaking countries and others heavily influenced by UK or US.

The macro-uniform, government-driven and tax-dominated class originated in the code law countries of continental Europe. It is also known as the Continental European model. It is used by most of Europe, Japan, and other code law countries. Companies in this group usually are tied quite closely to banks that serve as the primary suppliers of financing.

The inflation-adjusted model is found primarily in South America. This model distinguishes itself, however, though the extensive use of adjustments for inflation (Argentina, Brazil, Chile and Mexico).

The UK-influenced countries are former British colonialism on accounting development: Hong Kong, Malaysia, Nigeria, Philippines, South Africa, Singapore, Taiwan, Sri Lanka, Zambia, Botswana, Namibia, and Zimbabwe.

The macro-uniform countries and companies in the macro countries are more heavily influenced by taxation than are companies in the micro countries.

These factors were designed to operate for developed countries which share certain economic features. If one wished to include developing countries, it would be necessary to include other discriminating factors, such as the degree of development of economy or nature of economic systems.

Nobes (2006) showed the classification of some financial reporting systems. In this system ‘US GAAP’ means the well-defined set of practices required by US regulators to be used by certain US companies. Users of this system are SEC-registered US companies, and certain large Japanese companies for their group accounts. US GAAP bears a family resemblance to UK and IFRS rules, and is in a class of systems suited to strong equity markets.

Strong equity class covers UK, Irish, Dutch individual and US SEC-registered companies.

Weak equity class contains Belgian, French, German, Italian and Japanese enterprises.

Radebaugh and Gray (2002) presented the cultural classification of international accounting systems:

- anglo-american culture area (United Stated, United Kingdom and British colonials),
- nordic countries (The Netherlands, Sweden, Finland, Denmark),
- germanic accounting (Germany, Austria, Israel, Switzerland, and former European colonies in Africa),
- latin group (France, Italy, Brazil, Argentina, Belgium, Portugal, Spain, Chile, Columbia, Mexico, Peru, and Uruguay),
- asian accounting (China, Japan, India, Pakistan, Hong Kong, Singapore, Malaysia, and Philippines).

4. EUROPEAN ACCOUNTING SYSTEM

The European Union made efforts on harmonization of accounting standards of the member states through regulations, directives, official statements and recommendations in 1970’s and 1980’s. The intention of a common regulation of accounting and financial reports comes from the Treaty of Rome (25th March, 1957) which has defined the four freedoms, namely the free movement of goods, the free movement of capital, the free movement of persons and the free movement of services. Accordingly, the persons are free to settle down and start up new enterprises applying the national laws of the country of settlement. In order to meet the requirement of free movement of capital within the European Union, it is necessary to ensure the transparency and accuracy of accounting data. The obligation of financial reporting (Profit and Loss Account, Balance Sheet) and auditing helps the shareholders and stakeholders in decision making, facilitating the defence of their interests independently from the seat of the company (freedom of settlement).

The common regulation of accounting in the European Union is hierarchical. The basic rules are set down in company law. In the EU legislation system the law making function of the state is strictly separated from the application of law. The regulations are written down and there is a priority of Common Law respect to the national law.

4.1 Regulations

The regulations are obligatory and they come into force directly, without ratification of the member states. Regarding accounting standards one of the most significant regulations of the European Parliament and Council of the European Union is the 1608/2002 of 19th July, 2002. This regulation contains for instance that the companies registered on stock market from 2005 are committed to submit the consolidated financial statements compiled according to the IAS and IFRS. It is the member states' right to decide on whether they oblige the companies operating in their country to use IAS and IFRS when compiling their financial statements.

4.2 Directives

The directives are defining legal frameworks of the European Union, determining criteria and requirements to be met in national law therefore they seem to be long-term regulations. Directives referring to general accounting principles are as follows.

- *78/660/EEC 4th directive about the financial statement of companies;*
- *83/349/EEC 7th directive about the consolidated financial statement;*
- *86/635/EEC 8th directive about the certification procedure of the operation of certified public accountants in charge of supervision and audit of the financial statements.*

The directives contain the required minimum information of the financial statement, the compulsory structure of the Profit and Loss Account and of the Balance Sheet, the criteria of evaluation of assets, the definition of the rules of submitting simplified financial statement, and the way of publication.

The accounting directives aim at ensuring the accuracy and transparency, accordingly providing reliable information on the financial situation of a company. The Council of the European Union in conjunction with the European Economic and Social Committee codified that the *78/660/EEC* directive is to be applied in every member state's national law within a certain period of time.

4.2.1 Directive No. 4

This directive aims at ensuring the accurate, transparent overview of the financial situation of the companies for comparison between different member states' financial statements. The financial statements as a unit include the Profit and Loss Account, the Balance Sheet Account and the Notes to the financial statements in every member state. There are examples for application of simplified financial statements depending on the total value of assets, the revenues and the number of employees (when at least two out of three is under the limit in consecutive years). It is common in member states that the criterion of accounting fixed assets is the usage of it for long-term purposes. The distinction of extraordinary income and expenditure from operating income and expenditure applying the accrual policy is also a common procedure in the European Union. Additional common traits are the depreciation policy, the obligation of audit report as an annex of the financial statement, the publication and deposit of the financial statement.

4.2.2 Directive No. 7

Group of companies including the parent company and the affiliates operating in different countries are obliged to submit a consolidated financial statement. This directive ensures the financial comparability of such reports and makes it possible to show the group as a single corporation filtering the necessary transactions between the affiliates in order to present the accurate financial situation and performance of the group. In the member states the consolidated financial statement contains the consolidated Profit and Loss Account, the consolidated Balance Sheet and the consolidated Notes to the financial statement. It is common to filter the liabilities and the receivables between the consolidated companies so as the incomes and expenditures. The date of the affiliate's financial statement can coincide with the one of parent company.

4.2.3 Directive No. 8

This directive intends to establish congruence between the different regulations regarding the requirements towards the certified public accountants. It gives common guidelines for an auditor person and for an auditor company. The main elements of the directive are as follows:

- avoidance of incompatibility,
- adequate education and qualification requirements including practice,
- certification is to be a separate process for every single qualified person which guarantees the equal criteria for the auditor candidates.

The member states have to ensure that the certified public accountant be fair, independent, professionally updated.

4.3 Announcements

The official statements are not compulsory; they give guidelines for application of directives or complementary information on them such *as COM/2003/285* about the auditing or the *XV/7009/97* concerning the directives *78/660/EEC* and *83/349/EEC*, furthermore the *XV/D3/7002/97* regarding the introduction of EUR. There are official statements explaining the accounting of profit or loss due to exchange rate when converting a foreign currency. The overall function of official statements is to clarify some definitions of which interpretation differs in the member states.

4.4 Recommendations

The recommendations formulate solutions which are not obligatory, such as the recommendation in connection with the quality assurance of the auditing (*C/200/3004*) or about the independence of the certified public accountants (*C/2002/1873*). Furthermore, there is a recommendation on including the environmental issues into the annual report.

Europe is rich in well-tested, highly advanced accounting and controlling concepts. However, each accounting tradition has thus far been developed and applied more or less in a specific national context. A huge potential to shape the accounting and controlling practice globally remains unused and unexploited. I therefore propose a cooperation initiative that addresses all European controlling and accounting associations, as far as possible with the support of the European Union. Its mission:

- to bring the major players in the controlling and accounting scene in Europe together for such a pan-European initiative,
- to establish one European standard for accounting and controlling by combing the strengths of the different approaches,
- to take the lead in defining international accounting standards,
- to create enough momentum to attract non-European parties to join the initiative in a second step the development of a new proven 'best practice' in creating controlling, accounting and analytical data to

support managerial decision making based on an international accounting performance concept is at best still in its early stage. What I completely lack so far is analytical and accounting concepts based on the international performance-philosophy supporting by management in detailed day-to-day decision making.

5. THE INFLUENCING FACTORS OF ACCOUNTING HARMONIZATION

In order to standardize the different kind of financial statements, the International Accounting Standards Board is working on creating accounting principles which can be used in the whole world (Epstein and Mirza, 2007). Although the aim seems to be easy, the execution might be problematic due to the diversity of the current principles. The accounting harmonization establishes a system where the financial statements are standardized therefore they are transparent. However it does not mean that the use of standards would result in an operating consistent accounting system, because there are other factors which have influence on the harmonization process, for instance the national legislation system, the regulations by auditors or by the courts.

The reason for differences in accounting principles between certain nations could be that they vary in the level of economic development, in the legal system, in the taxation system, in the intensity of capital market, so as in the level of inflation, in the typical methods of financing an enterprise, in the shareholder background, finally in the political and cultural traits. These are all determining the regulatory aims and philosophy behind them.

5.1 Legal system

The legal system of a country mainly influences the accounting principles. There are two main clusters: the ‘civil law system’, based on codification (typical in almost all European countries except for United Kingdom and in Japan) and the so called ‘common law system’ which is precedent based (typical in the United Kingdom, in the USA). According to certain researches (e.g. Sodestrom and Sun, 2006) the principles of the financial reporting system and the accounting standards (especially regarding the principle of being careful or the discrete evaluation) differ very much from each other.

In the ‘civil law system’ the accounting standards are laid down in laws by the elected deputies. It is not common that companies in these countries (continental Europe and the historical colonies of Belgium, France, Germany, Italy, Portugal and Spain) are registered on stock exchange therefore the publication of financial statements is not a priority.

This system derives from the Roman Law (jus civile) the first description of which was the Codex Justinianeus in 529. The codification is done in accounting regulation as well (e.g.: the Hungarian Law of Accounting 100/2000.) however the company law contains the most important rules for the operation of a company such as the publication of the financial statement and its formal requirements. In such countries the accountant professionals motivate the introduction of the international accounting standards. In the ‘common law system’ only the frameworks are determined in the company law and the special regulation is done by the independent committee of accounting. Doing so, the committee focuses on the experience based solutions elaborating in details the accounting rules for profit oriented and non profit oriented companies.

In the ‘civil law system’ the Accounting Law is rather general, it does not contain special regulations, therefore if the companies face with special problems, they ask for help of auditors or search for other laws e.g. tax laws.

The ‘common law system’ develops much more detailed regulation. For the special cases common general rules are applied (in the USA, Canada, Australia or New Zealand). These countries are very market oriented and the investors trust much more in financial statements than in other states. The publication of this information is crucial. The regulation is clear and much more supporting the information needs of the shareholders, of stakeholders and of analysts. This is the best environment for international accounting standards.

5.2 Financing methods

The legal forms of companies and the proprietors are different. In Germany, in France, in Italy, the banks give the financial background. However in the United Kingdom or in the USA the companies are financed mainly by shareholders. Generally speaking, in the latter countries the capital markets are quite strong and there is a sounder defence of the shareholders. The company structure could be influenced by the political interests as well.

It is worthwhile to analyze the proprietors and the financing companies in the EU. In Germany it is common that banks own shares of the national companies and they are financing them at the same time. There are several national public limited companies in which Deutsche Bank has a significant portion of shares. The situation is similar in France and in Italy where the banks take part in decision making and in the execution of them too due to their significant amount of shares. In the United Kingdom and in the USA the main proprietors of national companies are rather the institutions than private shareholders. In the continental EU countries there are not many foreign shareholders, so for them it is not crucial to regulate the prompt publication of the financial statements there is no need for as much audit and the tax laws overwrite the accounting requirements. On the contrary the private financing system induce need for adequate accounting information, therefore the accounting rules are more separated from the taxation regulations and they are not in a hierarchical context. There is a strong need for more auditors.

5.3 Taxation system

In France and Germany the taxation laws function influenced the accounting rules. Belgium, Italy and Japan apply similar principles and the taxation laws have strong influence on the financial statements. In the USA and in the United Kingdom the accounting regulation totally differs from taxation regulations and they handle it by deferrals, calculating the difference between the tax payable according to accounting regulation and taxation regulation. This also applies to Holland. There are examples also in Hungary for deferrals of tax payable when it is about consolidation.

5.4 Inflation

The effect of inflation can be measured in connection with the evaluation of assets or when calculating the profit. The historical accounting principle of evaluation can cause problems in periods when there is a high inflation rate. The main problems come when a multinational company wants to make a consolidation in countries where there is a high inflation rate. The effects of inflation can be seen when evaluating the fixed assets or most directly when converting foreign currency. Measuring profitability can be done in the currency of the parent company or of the affiliate company. For instance, if there is an acquisition, the accounting of the goodwill is a crucial issue. According to the US GAAP after goodwill no amortization can be accounted; they calculate it through the net present value of the capability of producing income.

6. PROBLEMS CAUSED BY ACCOUNTING DIVERSITY

6.1 Preparation of consolidated financial statements

The diversity in accounting practice across countries causes problems that can be quite serious for some parties. One problem relates to the preparation of consolidated financial statements by companies with foreign operations. Consider General Motors Corporation, which has subsidiaries in more than 50 countries around the world. Each subsidiary incorporated in the country in which it is located is required to prepare financial statements in accordance with local regulations. These regulations usually require companies to keep books in local currency using local accounting principles. Thus, General Motors de Mexico prepares financial statements in Mexican pesos using Mexican accounting rules and General Motors Japan Ltd. prepares financial statements in Japanese yen using Japanese standards. To prepare consolidated financial statements into U.S. dollars, the parent company must also convert the financial statements into U.S. dollars and the parent company must also convert the financial statements of its foreign operations into U.S. GAAP. Each foreign operation must either maintain two sets of books prepared in accordance with both local and U.S. GAAP or, as is more common, reconciliations case, considerable effort and cost are involved company personnel must develop an expertise than one country's accounting standards.

6.2 Asses to foreign capital markets

A second problem caused by accounting diversity relates to companies gaining access to foreign capital markets. If a company desires to obtain capital by selling stock or borrowing money in a foreign country, it might be required to present a set of financial statements prepared in accordance with the accounting standards in the country which the capital is being obtained. Consider the case of the Swedish appliance manufacturer AB Electrolux. The equity market in Sweden is so small (there are fewer than 9 million Swedes) and Elektrolux's capital needs are so great that the company has found it necessary to have its common shares listed on stock exchanges in London and on the NASDAQ in the US, in addition to its home exchange in Stockholm. To have stock traded in the US, foreign companies must either prepare financial statements using U.S. accounting standards or provide a reconciliation of local GAAP net income and stockholders equity to US GAAP. This can be quite costly. In preparing for a New York Stock Exchange (NYSE) listing in 2008, the German automaker Daimler-Benz estimated it spent $ 120 million to initially prepare U.S. GAAP financial statements, it expected to spend $30 to $40 million each year thereafter.

6.3 Comparability of financial statements

A third problem relates to the lack of comparability of financial statements between companies from different countries. A lack of comparability of financial statements can have an adverse effect on corporations when making foreign acquisition decisions. There was a very good reason why accounting in the communist countries of Eastern Europe and the Soviet Union was so much different from accounting in capitalist countries. Financial statements were not prepared for the benefit of investors and creditors to be used in making investment and lending decisions. Instead, financial statements were prepared to provide the government with information to determine whether the central economic plan was being fulfilled. Financial statements prepared for central planning purposes have limited value in making investment decisions.

6.4 Lack of high-quality accounting information

A fourth problem associated with accounting diversity is the lack of high-quality accounting standards in some parts of the world. There is general agreement that the failure of many banks in East Asian financial crisis was due to three factors:

- a highly leveraged corporate sector,
- the private sector's reliance on foreign currency debt, and
- lack of accounting transparency.

International investors and creditors were unable to adequately assess risk because financial statements did not reflect the extent of risk exposure due to the following disclosure deficiencies:

- the actual magnitude of debt was hidden by undisclosed related-party transactions and off-balance-sheet financing,
- high levels of exposure to foreign exchange risk were not evident,
- information on the extent to which investments and loans were made in highly speculative assets was not available,
- contingent liabilities for guaranteeing loans, often foreign currency loans, were not reported, and

- appropriate disclosures regarding loan loss provisions were not made.

7. CONCLUSIONS

The present impetus for global accounting information system follows the accelerating integration of the world economy. The application of international financial reporting standards will allow greater comparison of international financial results. The unified accounting information system will probably lead to new types of analysis and data; furthermore, with the possible integration of new indicators from the practice of certain countries.

The accounting information system differences matter even to financial analysts who specialize in collecting, measuring and disseminating business information about the covered companies suggests that there are potential economic costs, associated with variation in national rules across countries. Besides, it is very important task for managers and researchers the valuation and analyzing the effects of international accounting standards on the business environment, especially their contribution to harmonization and globalization. While a large body of this study is devoted to understanding the causes and consequences of the adoption of international accounting standards, researcher' attention has thus, far focused almost exclusively on the informational benefits for the business environments, like evolution of business turnover, employees and the management performance.

There is certainly empirical research evidence to support the notion that uniform accounting standards will increase market liquidity, decrease transaction costs for investors, lower cost of capital, and facilitate international capital formation and flow. Reduced costs will also result in more cross-listings and cross-border investments. International standards also have a good effect on the division of labour too. And there is a sufficient basis to endorse international standards and begin the challenging task of educating users, auditors, and regulators. Educators and practicing accountants alike have significant roles to play in this exciting future.

Harmonization of financial accounting has tended to follow the integration of the markets served by the accounts. The global accounting standards would enable the world's stock markets to become more closely integrated. The more closely world's stock markets approach a single market, therefore, the lower should be the transaction costs for investors and the cost of capital for firms in that market. The differences in international reporting practice prior to IFRS constituted a palpable barrier to efficient international investment, monitoring and contracting. Literature suggest that being confined to small segmented capital markets imposes a substantially larger cost of capital on firms and transaction costs on investors, which would inhibit much worthwhile investment. Although we do not have all elements for the cost-benefit calculation, the evidence points to substantial net gains for smaller economies which have joined to the IFRS regime. There is certainly empirical research evidence to support the notion that uniform financial reporting standards will increase market liquidity, decrease transaction costs for investors, lower cost of capital, and facilitate international capital formation and flow. And there is a sufficient basis to endorse IFRS and begin the challenging task of educating users, auditors, and regulators. Educators and practicing accountants alike have significant roles to play in this exciting future.

Unified international accounting system creates more transparency on the financial market. This provides investors more accurate information on company profiles. This way, even small investors (and not only professionals) will be able to get the information needed for their investment choices, thus they will be able to better compete on the market. More transparency will result in more international transactions that will have reduced costs because of the clear information provided by companies' reports. In case of consolidated accounts (when the company has foreign subsidiaries) bookkeeping will be facilitated and will also result in reduced transaction costs. No more adjustments will be needed in order to make financial reports of companies internationally comparable. Reduced costs will also result in more cross-listings and cross-border investments. International accounting standards also have a good effect on the division of labour. These standards and thus the less transaction costs will enable companies to be able to trade easier between each other. This will let them specialise in the field of their strengths and rather rely on suppliers that are also specialists in another field of their own than trying to produce the same product in-house, which will create a division of labour on the market. Accounting standards also provide information on company disclosure. Better transparency, by providing more information, and providing the accurate and understandable information will reduce the risk perceived by investors. The risk in question is the accounting risk that comes from the difficulties in understanding the accounting principles and standards applied by the firm, and also the inability of investors to process the information provided. By reduced risk investors will get lower returns from their investments that will result in lower cost of capital as well. Businesses that are using IFRS face less earning management, more earnings and more value relevance of earnings. This can be due to the easier flow of capital, the less costs attributable to the difficulties of adjusting the reports of companies from different accounting systems. Due to the decreasing costs of processing the information provided in financial statements the efficiency of stock markets will increase which will result in greater prices of stocks and thus greater capital income for enterprises. These all will provide space for more innovation on the financial markets because they could become more integrated, and more and new international transactions could be created. Due to accounting standards, the international flow of capital will be easier.

It seems to be apparent that the appropriate international accounting system contributes to the division of labour, to financial innovation and to the reduction of the cost of capital and even to the increase of the businesses' earnings. The first argument for the harmonization of accounting standards is the existence of the multinational companies, who invest enormous efforts into the preparation of their financial statements in order to comply with the national standards. For these companies life would be much easier if the same rules would apply to their subsidiaries all around the world. On the other hand this would be profitable for the investors as well, as they could compare the enterprises' results without difficulties, which would spare both money and other resources for them. This would also lead to the reduction of the information asymmetry between managers and investors. The information asymmetry is a costly thing which can be blamed for the increase of the equity's cost and the inaccuracy of the economical and the financial forecasts. So the aim of the international accounting systems is that similar transactions are treated the same way all around the globe which enables the creation of unified financial statements.

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